



Hawaii Employer-Union Health Benefits Trust Fund

Special Report Evaluating the Implementation, Administration & Financial Impact of New Benefit Plans Which Began on July 1, 2003

October 22, 2003

Garner
Consulting



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October 22, 2003

Board of Trustees
Hawaii Employer-Union Health Benefits Trust Fund
P.O. Box 2121
Honolulu, HI 96805

Re: Report on Implementation, Administration and Financial Implications

Dear Board Members:

Garner Consulting is pleased to submit this report on the implementation, administration and financial implications of the new benefit plans which began on July 1, 2003.

We look forward to discussing this report with you

Sincerely,

A handwritten signature in black ink, appearing to read "John C. Garner", is written above the typed name.

John C. Garner, CEBS, CLU, CFCI, CPCU
Chief Executive Officer

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EXECUTIVE SUMMARY

This special report evaluates the activities of the Hawaii Employer-Union Health Benefits Trust Fund ("EUTF") related to the new benefit plans effective July 1, 2003.

The Board of Trustees selected Garner Consulting as its benefit plan consultant and hired Mark Fukuhara as Administrator in June 2002 and July 2002. From that point forward, all activity was focused on designing benefit plans, selecting vendors and conducting open enrollment for the July 1, 2003 effective date. The Board gave its final approval of insurance carrier selections, plan designs and rates in March 2003.

Implementation

There were significant problems in the implementation process. Some of the problems were related to the delay in final approval of the carriers, plans and rates by the Board, which negatively impacted the open enrollment process. Other problems were related to the change from PEHF to the EUTF, such as the numerous rumors and misinformation that circulated regarding the change.

The EUTF did learn a number of lessons from this open enrollment period. We do believe the EUTF staff did the best job possible with the time and resources available.

Administration

The EUTF has already made significant improvements compared to the PEHF. We believe the EUTF forms are more user friendly than the PEHF forms. The EUTF is also structured to provide needed senior and middle management that was lacking with the PEHF. The EUTF administrative rules also incorporate a number of changes that have streamlined workflow.

All the administrative issues may be academic if the Board decides to outsource benefit administration to a third party. If the Board does not decide to outsource all administration, a number of changes will be needed.

Financial Impact

We analyzed the financial impact of the EUTF plans by comparing EUTF rates to rates for the PEHF, had it been extended for one year, and to national trends. These rate differentials were applied to the September 30, 2003 enrollment figures to arrive at total impact. Our analysis included rates, the impact of benefit enhancements and administrative savings from carriers.

We estimate that total savings for actives employees are \$9,356,408 and for retirees are \$7,342,926, for a grand total of \$16,699,334 or 3.51% of total premiums of \$475,772,426. Of these savings, we estimate that \$1,985,179 is due to administrative savings from carriers. These savings offset 57% of the EUTF operating budget.

BACKGROUND

This special report evaluates the activities of the Hawaii Employer-Union Health Benefits Trust Fund (“EUTF”) related to the new benefit plans effective July 1, 2003.

The EUTF was created by Act 88, 2001 Session Laws of Hawaii, and replaced the Public Employees Health Fund (“PEHF”) on July 1, 2003. The EUTF was established to provide a single delivery system of health benefits for State and County employees, retirees and their dependents that is affordable to both public employers and participants. The intent of combining all public employees into a single health benefits program was to increase negotiating leverage with health benefits carriers and create economies of scale through the consolidation of administrative functions.

Act 88, SLH 2001, enacted major reforms in the administration of the public employee health fund. Some of the significant changes are:

- A defined contribution plan for retirees is established with capped employer contributions that are adjusted annually based upon changes in Medicare Part B premium amounts.
- Public employers’ contributions for active employees are a specific dollar amount as negotiated through collective bargaining.
- Employees who were hired on or after July 1, 2001 will receive an employer contribution for only the employee’s coverage upon retirement.
- The Board of Trustees has equal representation of public employer and employee-beneficiary trustees, including a retiree representative.
- The retention of auditors, actuaries, investment firms and managers, benefit plan consultants, or other professional advisors to carry out the purpose of the fund is exempt from Chapter 103D, HRS, procurement requirements.
- The EUTF Administrator and new staff positions are exempt from civil service.
- Health benefits plan monthly premiums include the administrative expenses of the EUTF.

The Board chose Garner Consulting as its benefit plan consultant in June 2002 and hired Mark Fukuhara as Administrator in July 2002. Mr. Fukuhara hired staff that includes an assistant administrator, secretary, financial management officer, communications and regulatory specialist and information systems analyst. The Administrator and staff of the EUTF assumed the functions of the PEHF, including the transfer of PEHF assets, positions and staff effective July 1, 2003.

A request for proposals (RFP) was issued September 6, 2002 soliciting proposals for medical, prescription drug, vision, dental and life insurance to be effective July 1, 2003. Proposals were received from carriers by the deadline of October 1, 2002 and were evaluated by the Benefits Consultant. The intent was to have the recommended plans and associated premiums approved by the Board by December 2002.

However, the Board and its subcommittees were unable to convene meetings from mid-October 2002 until late January 2003 due to lack of quorum. Quorum for Board meetings requires a minimum of three employee-beneficiary trustees and three employer trustees.

The Board gave its final approval of insurance carrier selections, plan designs and rates in March 2003.

IMPLEMENTATION

There were significant problems in the implementation process. Some of the problems were related to the delay in final approval of the carriers, plans and rates by the Board. Other problems were related to the change from PEHF to the EUTF, such as the numerous rumors and misinformation that circulated regarding the change.

In an effort to educate as many employees as possible about the changes in benefits, the EUTF requested that employees be given time off to attend open enrollment meetings. The Board of Education did not grant its employees time off, but the EUTF arranged meetings after school at many schools around the Islands.

Because of the delays mentioned above, there was also a delay in scheduling open enrollment meetings. By the time meetings were scheduled, many of the larger venues had already been booked, which resulted in overcrowded sessions in smaller locations.

Even though the EUTF staff anticipated larger attendance at meetings than the PEHF had experienced in the past, no one predicted the overwhelming attendance, particularly early in the open enrollment period. Therefore, there were logistical problems with inadequate meeting sites and meeting space. The EUTF responded by scheduling additional meetings later in the open enrollment period, particularly at larger venues. The open enrollment sessions were generally communicated as two-hour time blocks, but in fact multiple sessions were held during those times.

There were also allegations of inaccurate and disparaging remarks made by the presenters about the role of public sector unions and the Trustees in the implementation of the EUTF. Garner Consulting sent a representative to open enrollment meetings and can report that no such disparaging remarks were made at any of the meetings Garner Consulting attended.

There were also significant problems with telephone communications. The number of phone lines and staff available to handle the volume of calls was inadequate. The EUTF added telephone lines and staff to handle the telephone calls and returned calls in the evenings and on weekends. The EUTF staff and volunteers worked long hours to answer and return calls and emails, but the number of inquiries was overwhelming.

The fax machine was also overloaded and EUTF management attempted to install two additional fax machines to provide greater capacity, but the numerous steps required to execute this delayed the installation long enough to cause a high level of frustration for DPOs attempting to fax forms to the EUTF.

There were also problems related to enrolling students. The EUTF did not have the demographic information from the employee organizations that would have facilitated the process. In addition, miscommunication with ICSD data entry personnel caused programming problems with the actual enrollments. These resulted in incorrect confirmation notices, which in

turn resulted in inquiries from employees and required additional data entry and second confirmation notices. Finally, the imaging system was not functional until after open enrollment, so, once the problems were identified, it was difficult for EUTF staff to proactively retrieve the “processed” forms and correct them.

Some departments also experienced difficulties that were not the fault of the EUTF. Some departments, in an effort to be helpful to their employees, became bottlenecks as they required all forms to come through the department and be copied. The EUTF instructed Departmental Personnel Office (DPO) staff to discard PEHF forms as they were replaced with EUTF forms. This applied initially to enrollment and COBRA forms. They were also instructed to check the EUTF website for new forms as they became available. Some DPO staff misunderstood the instructions and discarded all PEHF forms, as well as some non-PEHF forms and manuals that relate to benefits, such as Premium Conversion Plan forms.

The EUTF did learn a number of lessons from this open enrollment period. We do believe the EUTF staff did the best job possible with the time and resources available.

In the future, it should not be necessary to give employees time off to attend open enrollment meetings. It will probably be sufficient to schedule meetings primarily during evenings and weekends.

With regard to the allegations of disparaging remarks, it is possible that a statement of fact could be interpreted as disparaging. For example, it is true that the Trustees were responsible for making the decision to have two tiers of rates. The Trustees made this decision based on a study that showed this rate structure would negatively impact fewer people than any other alternative, but the presenter may not have been aware of the study. Similarly, the unions are responsible for what they negotiated. We do not believe it is the place of the EUTF to point out other trade-offs that may have been made, such as previously negotiating higher salaries in lieu of higher contributions toward benefits. We recommend a more scripted approach to presentations in the future, as well as scripted answers to questions. We also recommend exploring other alternatives, such as videotaping a session and making the video widely available. This would assure that everyone receives the same message and that it is free of any disparaging remarks.

We also recommend attempting to schedule larger venues as soon as possible in the future and doing a better job of communicating the times of the sessions. Beginning planning and preparation earlier will allow for a smoother open enrollment. In order to do so, it will be necessary for the Board to finalize rates and benefits by December or January, rather than March.

ADMINISTRATION

The EUTF inherited many of the PEHF's processes with the PEHF staff. The PEHF work processes and operations rely on approximately 500 front-line State and County DPO staff who work directly with their respective departmental employees to collect the necessary enrollment data that is required to provide the employees health and life benefits. The DPO staff provides information to employees regarding the health and life insurance plan options, specific EUTF enrollment requirements and applicable enrollment deadlines.

The EUTF has already made significant improvements compared to the PEHF. We believe the EUTF forms are more user friendly than the PEHF forms. The EUTF is also structured to provide needed senior and middle management that was lacking with the PEHF. The EUTF administrative rules also incorporate a number of changes that have streamlined workflow.

The current paper-intensive, manual enrollment process results in too many possible points where enrollments can be delayed, misplaced or lost. Because the current process is a paper-based process, it means that DPO staff does not have on-line access to enrollment data. The PEHF did not have reference documents on its various, complicated processes.

There are also problems related to the structure of the Health Fund Information Management System (HFIMS). Apparently, the PeopleSoft system was customized for the PEHF to fit old, paper-based processes, rather than re-engineering the processes to take advantage of the system.

Not all of the PEHF staff that the EUTF inherited are fully trained and capable of providing the services that are needed. For example, we understand that some staff have resisted becoming computer literate, based on outdated job descriptions that make no reference to computer use.

All the administrative issues may be academic if the Board decides to outsource benefit administration to a third party. If the Board does not decide to outsource all administration, a number of changes will be needed.

We believe the most important change would be to replace HFIMS with an Internet-based system that would also allow employees to make their own benefit elections and changes on-line (this is generally known as employee self-service). Such a system would either allow EUTF to bypass the DPO staff (which can be a bottleneck) or give the DPO staff access to the system, which would enable the DPO staff to perform their functions in a more accurate and timely manner. Good systems of this nature also include a number of edits and prompts to assure accurate data entry. These systems also could be structured to capture personnel actions from payroll and departmental human resource systems. This would enable the EUTF to reduce data entry related to new hires, terminations and transfers and to eliminate redundant data entry of demographic and employment data.

Changing from HFIMS to an Internet-based system should be accompanied by a re-engineering of the workflow in the EUTF office to take full advantage of the computer system. Sustained

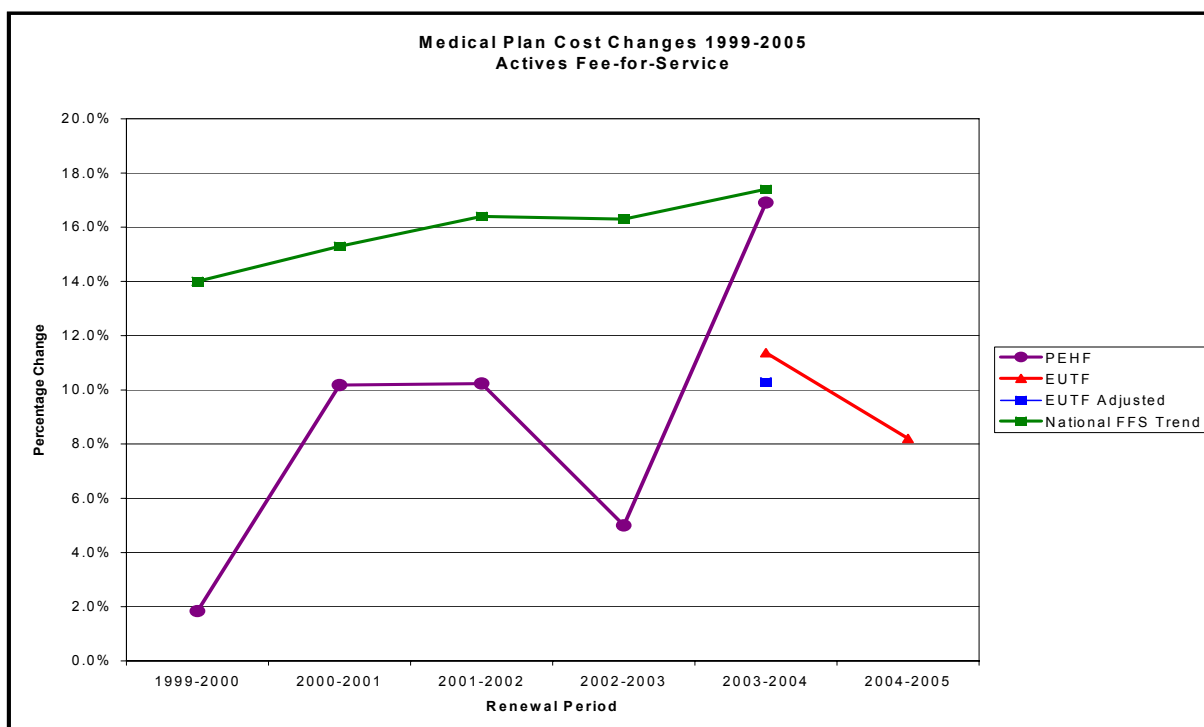
vision, leadership, commitment and support will be needed to keep any re-engineering effort on track. We believe the current EUTF management is capable of providing such vision and leadership. The Board would have to provide commitment and support in order for re-engineering to be successful.

The old PEHF staff will need to be trained in order to provide necessary service, either under the current system or with an Internet-based system. New job descriptions will be needed if benefits administration is not outsourced.

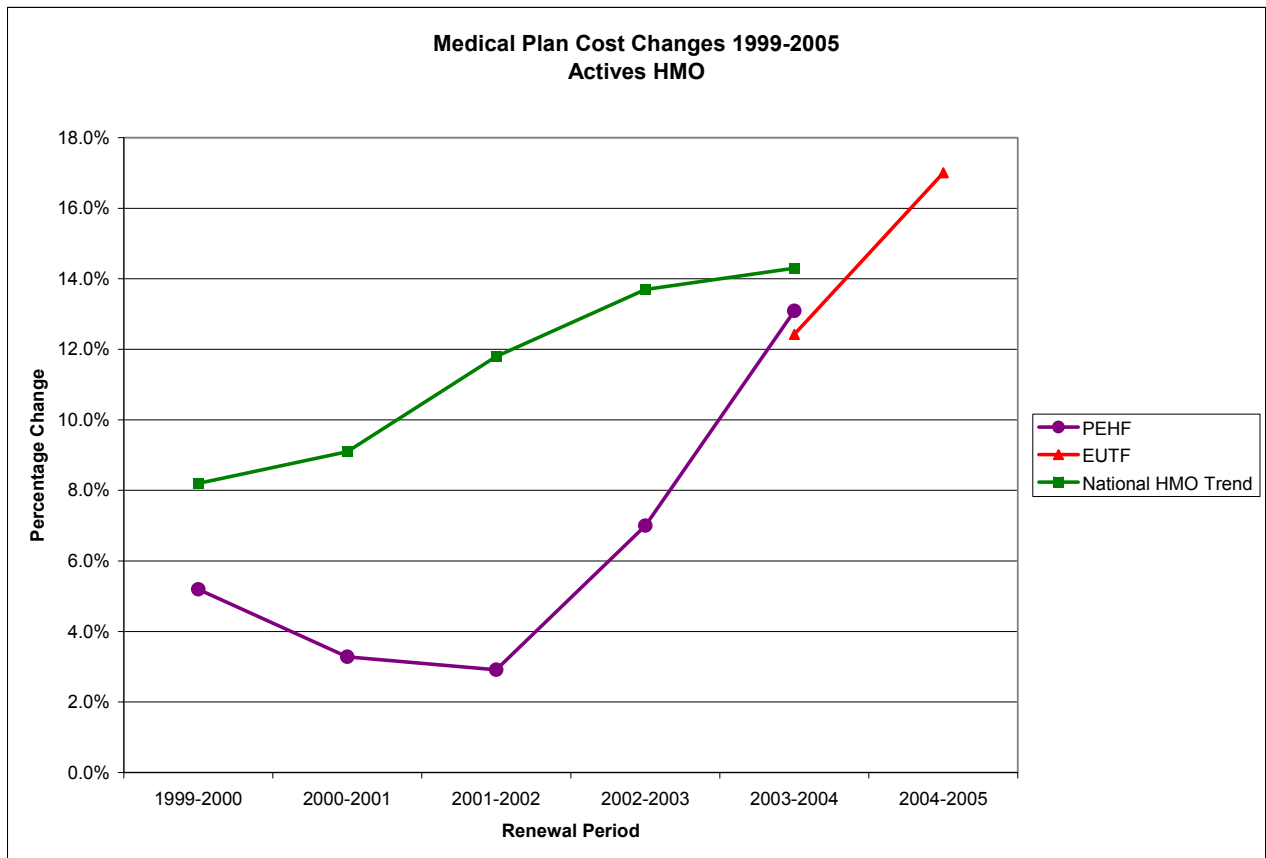
FINANCIAL IMPACT

We analyzed the financial impact of the EUTF plans by comparing EUTF rates to rates for the PEHF, had it been extended for one year, and to national trends. These rate differentials were applied to the September 30, 2003 enrollment figures to arrive at total impact. The graphs in this section display the annual percentage change in premiums for the Health Fund from the 1999-2000 fiscal year through the 2002-2003 fiscal year and the Trust Fund's premiums for the 2003-2004 and 2004-2005 years. The graphs also show what the PEHF rates would have been for the 2003-2004 plan year. These graphs also show the national trends, as reported in various published surveys. There are separate graphs for active employees, retirees with Medicare and retirees without Medicare. There are also separate graphs for HMSA and Kaiser.

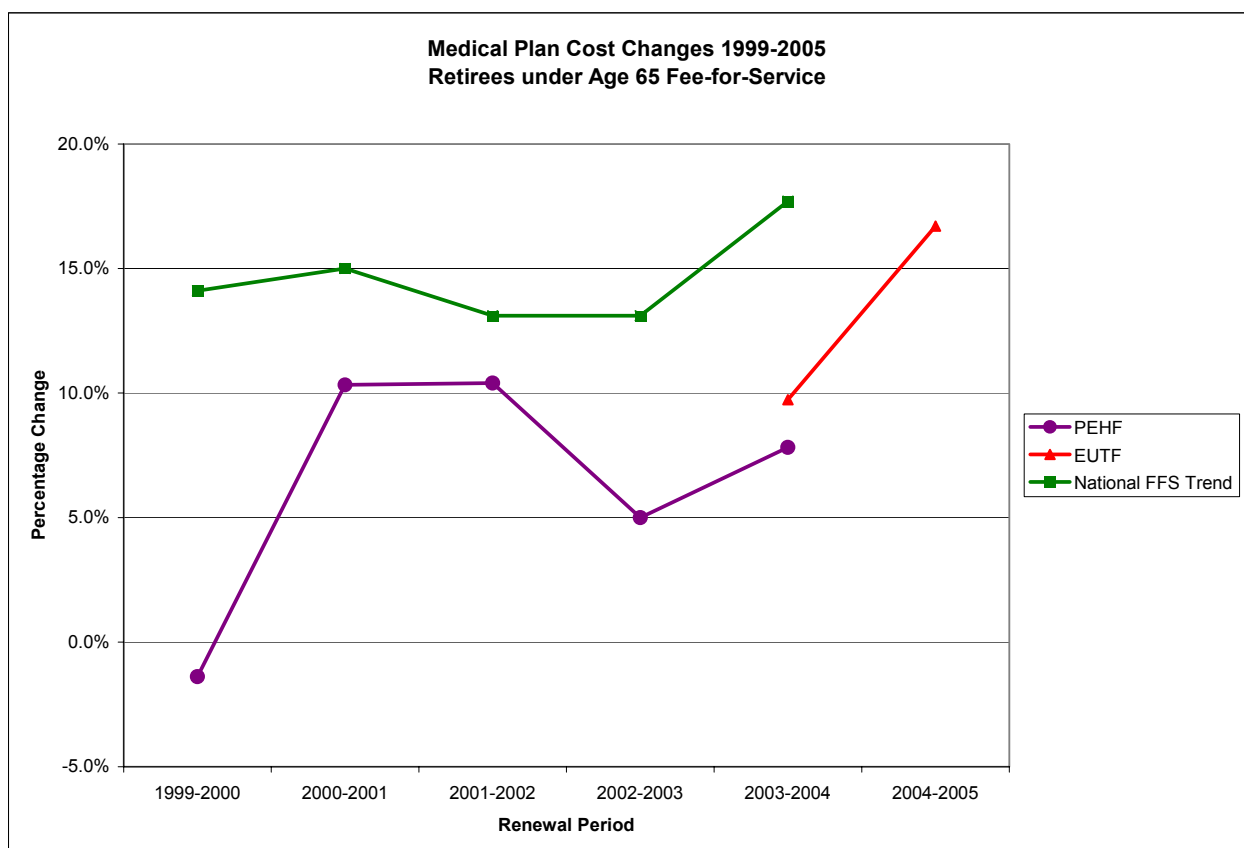
The first graph shows HMSA's rate increase percentages for active employees compared to national trend data for fee-for-service plans. PEHF rate increases were consistently well below national averages, but would have been close to the national average if the PEHF had been extended for another year. The EUTF rates are 5% less than the PEHF rates would have been. The point labeled "EUTF Adjusted" reflects Garner Consulting's estimate of what the rate increase should have been if the EUTF had not improved benefits. The largest improvement in benefits, compared to HMSA's determination of a PPO plan that was the actuarial equivalent to the PEHF plan, was a decrease in the out-of-pocket limit. HMSA agreed in its proposal to limit the second-year increase to less than 15%. At this point in the negotiations, HMSA has agreed to limit its rate increase in the second year of the contract to 8.2%. The total first-year savings are \$10,302,946, which is about 4.95% of the annual premium.



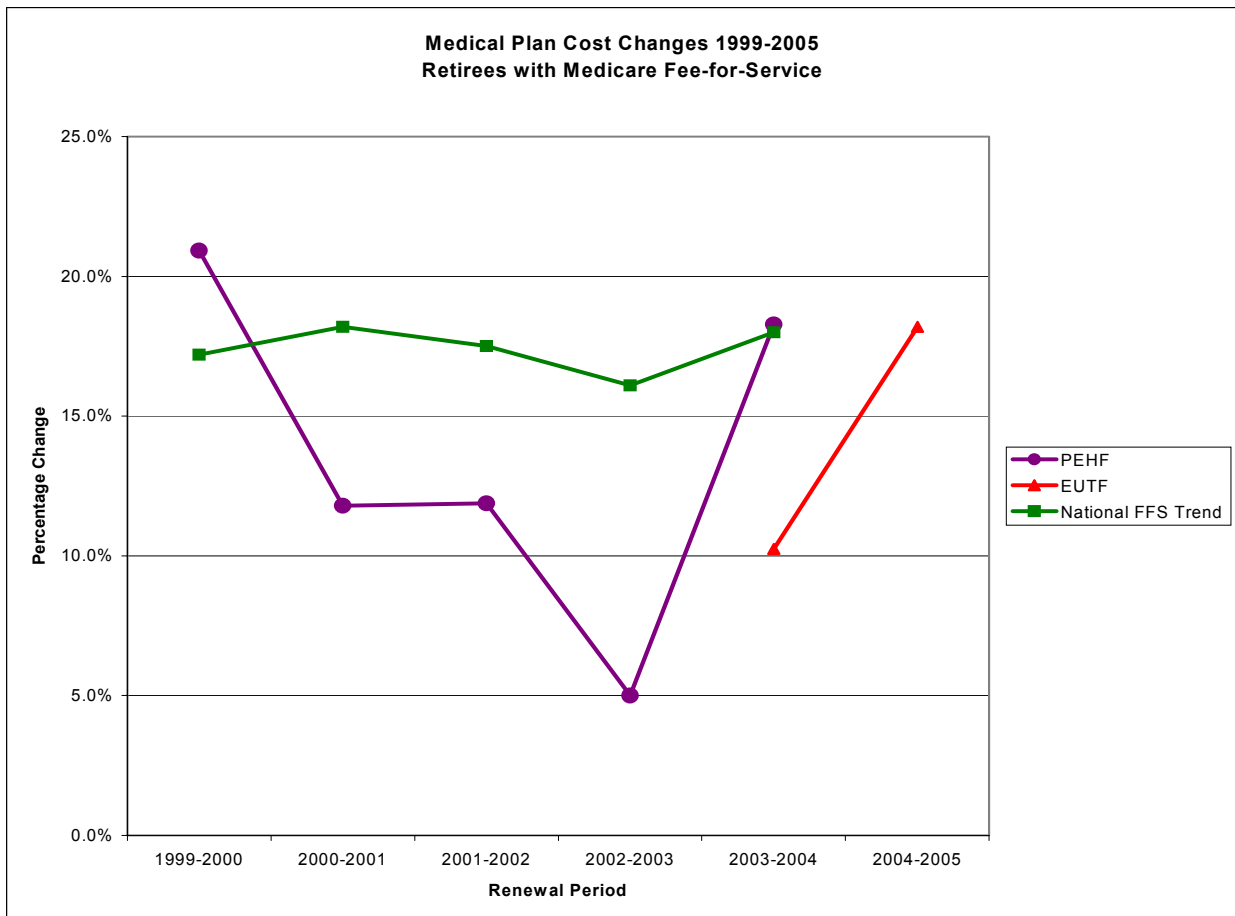
The next graph shows Kaiser's rate increase percentages for active employees compared to national trend data for HMOs. PEHF rate increases were well below national averages, but would have been close to the national average if the PEHF had been extended for another year. The EUTF rates are about 0.5% less than the PEHF rates would have been. The EUTF rates for the 2004-2005 plan year are subject to change, but Kaiser had previously guaranteed that the second-year rates would not increase by more than 36.2%. At this point in our negotiations, Kaiser has agreed to hold the second-year rate increase to 17%. Because the EUTF does not have an experience-rated contract with Kaiser, we cannot identify economies of scale separately from any other factors that generate savings. The first-year savings, compared to the PEHF are \$354,481, which is approximately 0.6% of the annual premium.



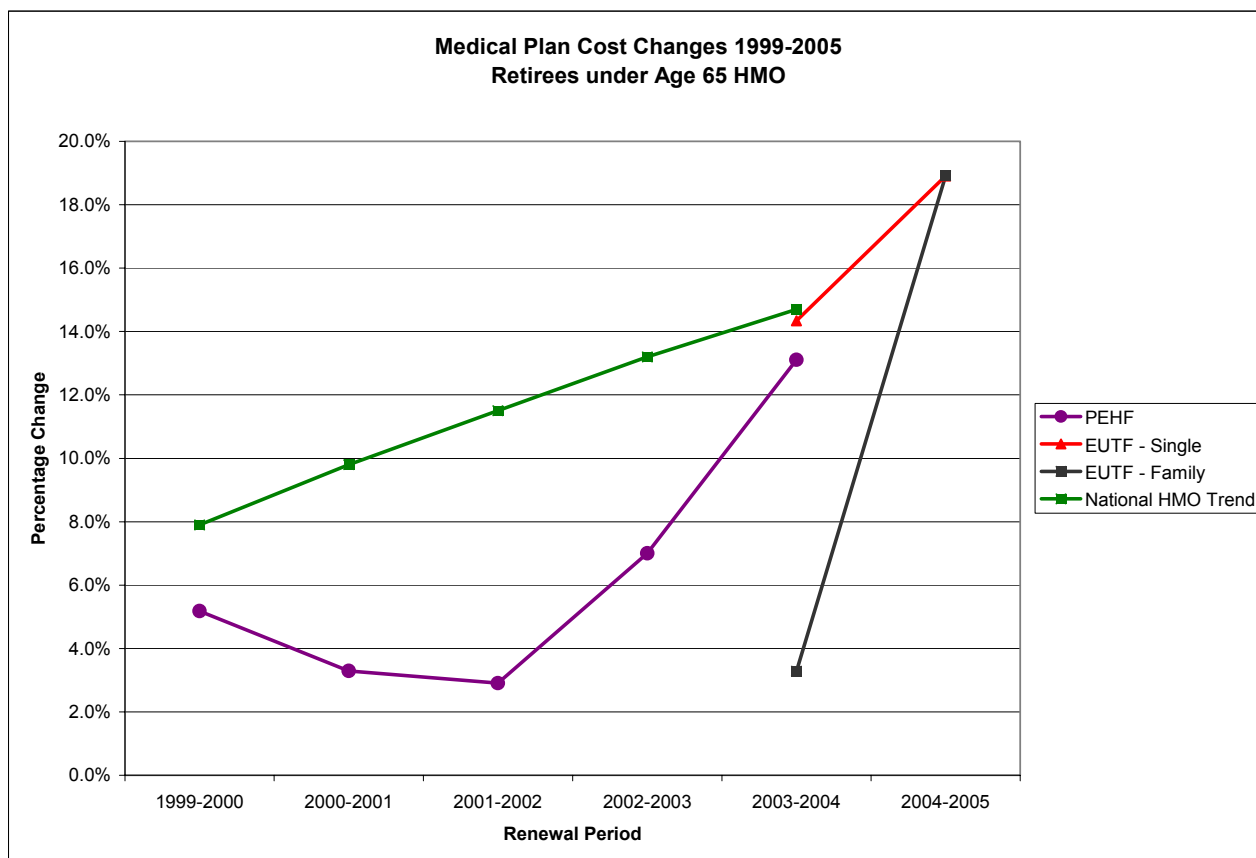
Next, HMSA's rate increase percentages for retirees without Medicare are shown compared to national trend data for fee-for-service plans. PEHF rate increases were below national averages. The EUTF rates are about 1.7% higher than the PEHF rates would have been, which we believe represents an overly conservative underwriting position on the part of HMSA. Because of the experience-rated arrangement EUTF has with HMSA, the EUTF should receive a return of surplus after the annual accounting, if we are correct that HMSA has been overly conservative. The EUTF benefits for retirees are slightly better than those provided by the PEHF. We believe the value of the improvements (the major change was increasing the lifetime maximum to \$2,000,000) is less than half a percent and have not shown an adjusted amount. HMSA agreed in its proposal to limit its increase for the second year of the contract to 17.7%. At this point in our negotiations, HMSA has agreed to no more than a 16.7% increase. The total first-year increase in cost is \$861,941.



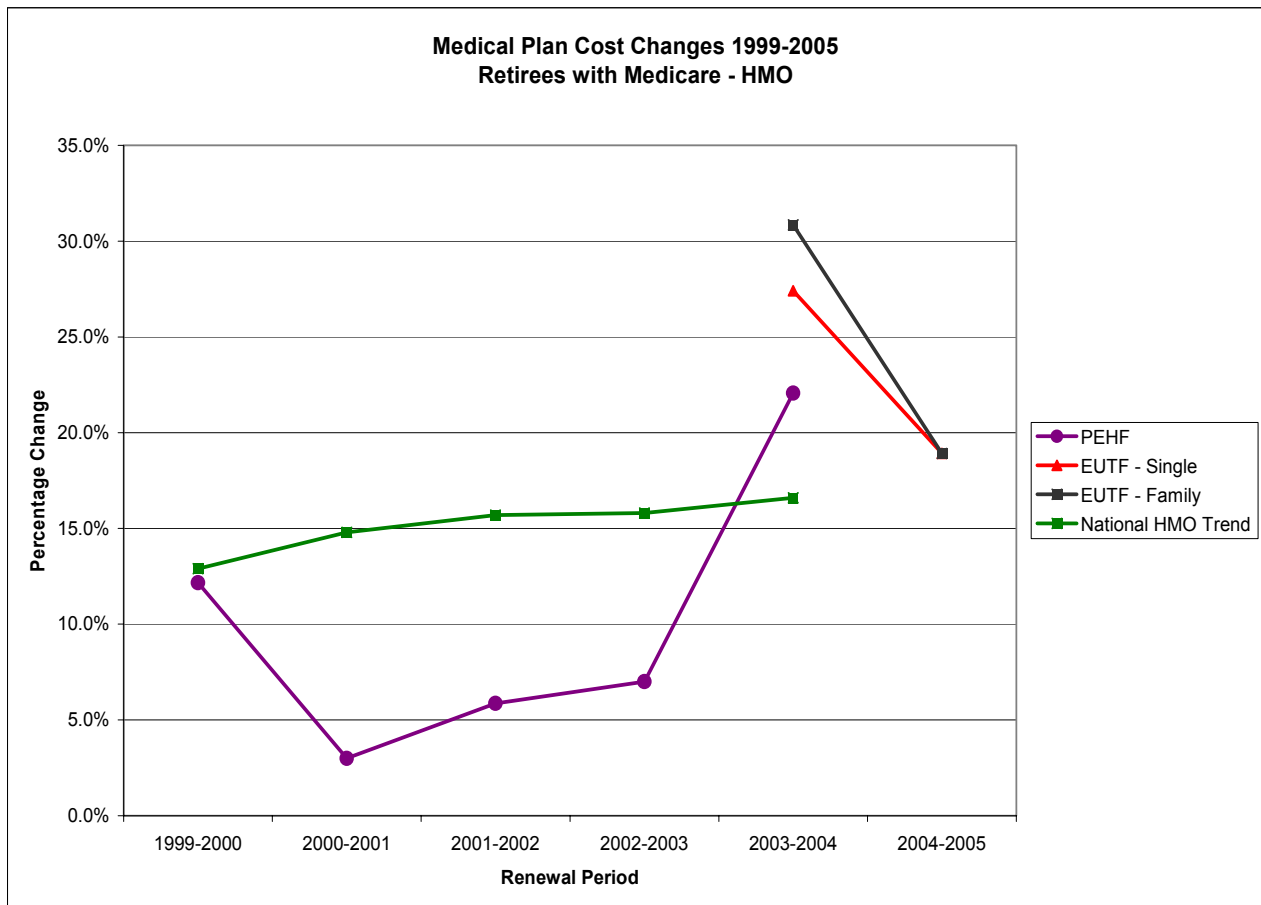
The graph below shows HMSA's rate increase percentages for retirees with Medicare compared to national trend data for fee-for-service plans. PEHF rate increases in recent years were less than national averages, but would have been higher than the national average if the PEHF had been extended for another year. The EUTF rates are 7.5% less than the PEHF rates would have been. The EUTF benefits for retirees are slightly better than those provided by the PEHF. We believe the value of the improvements (the major change was increasing the lifetime maximum to \$2,000,000) is less than half a percent and have not shown an adjusted amount. HMSA agreed in its proposal to limit its increase for the second year of the contract to 18.7%. At this point in our negotiations, HMSA has agreed to no more than an 18.2% increase. The total first-year savings are \$6,534,653.



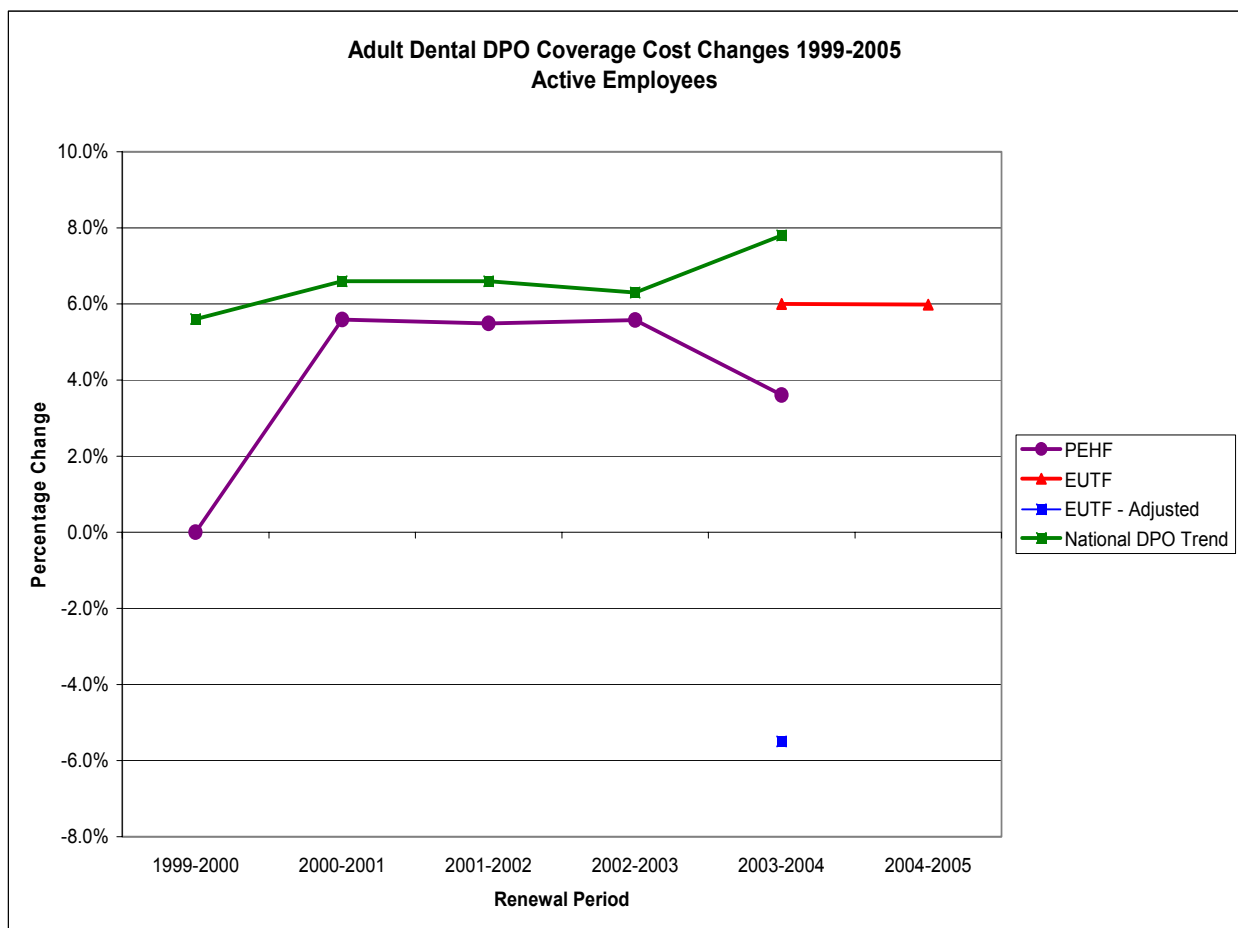
Kaiser's rate increase percentages for retirees without Medicare, compared to national trend data for HMOs, are shown below. PEHF rate increases have been consistently less than national averages. At our request, Kaiser reallocated its rates to stay within Act 88's rate caps. Therefore, we have shown the EUTF rate increases separately for single and family coverage. As the graph shows, Kaiser's single rate increase for EUTF was higher than the PEHF increase would have been, but the rate increase for retirees with family coverage was significantly less. The EUTF rates for the 2004-2005 plan year are subject to change, but Kaiser had previously guaranteed that the second-year rates would not increase by more than 22.8%. At this point in our negotiations, Kaiser has agreed to hold the second-year increase to 18.9%. We estimate that the first-year savings compared to the PEHF are \$790,136; a savings of 6.7%.



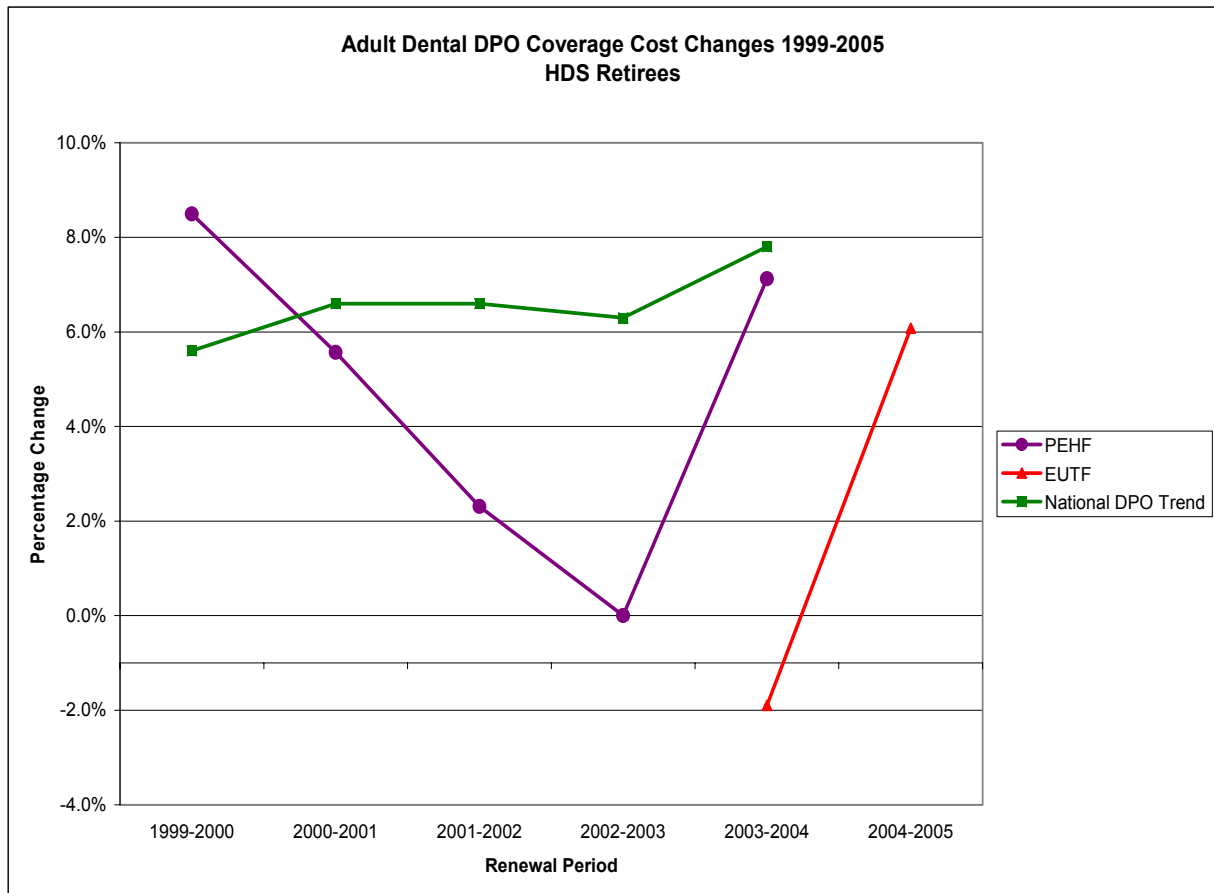
The graph below shows Kaiser's rate increase percentages for retirees with Medicare compared to national trend data for HMOs. PEHF rate increases have been less than national averages, but would have been higher if the PEHF had been extended for another year. EUTF rates are higher than the PEHF rates would have been. We believe this reflects both the different times at which PEHF requested rates and when EUTF finalized rates and a reallocation of retiree rates to stay below the caps. The EUTF rates for the 2004-2005 plan year are subject to change, but Kaiser had previously guaranteed that the second-year rates would not increase by more than 22.8%. At this point in our negotiations, Kaiser has agreed to hold the second-year increase to 18.9%. We estimate that the first-year additional cost compared to the PEHF is \$848,317.



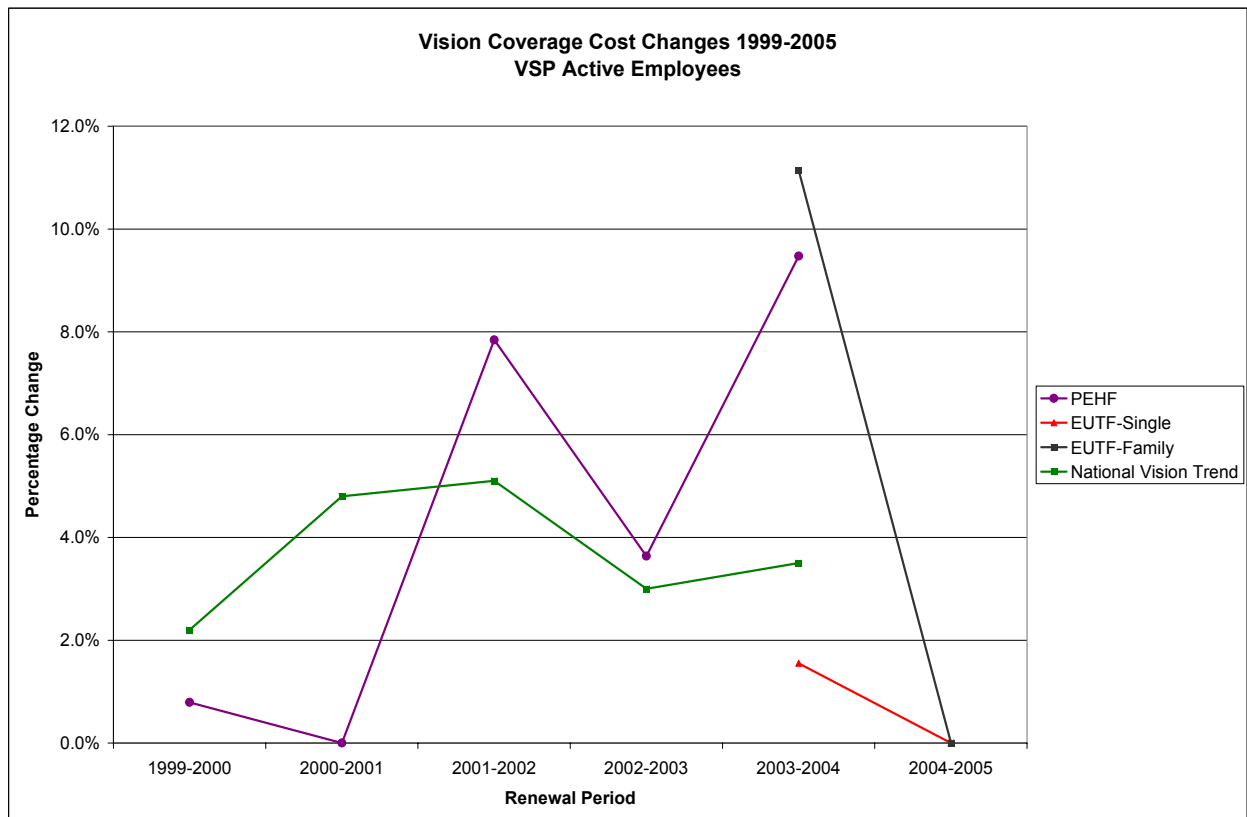
This chart shows Hawaii Dental Service's rate increase percentages for active employees compared to national trend data for dental plans. PEHF rate increases were slightly less than national averages. The actual EUTF increase was more than the PEHF increase would have been, but Garner Consulting estimates that the EUTF rates should have decreased if it were not for the dental plan improvements. Garner Consulting estimates that the EUTF dental plan for active employees is 10.8% better than the PEHF plan. The major improvements in benefits were increasing the annual benefit maximum from \$1,000 to \$2,000, adding an orthodontia benefit and improving the benefit percentage for minor restorative services from 60% to 80%. We added children's coverage to the family plan (rather than having a separate children's dental plan) and improved the benefits at a total first-year cost, compared to the PEHF, of \$335,068. Because of the consolidation of the adult and children's dental plans, comparisons with PEHF are difficult. We based our estimate of savings on the rate for single employees, which probably understates the savings.



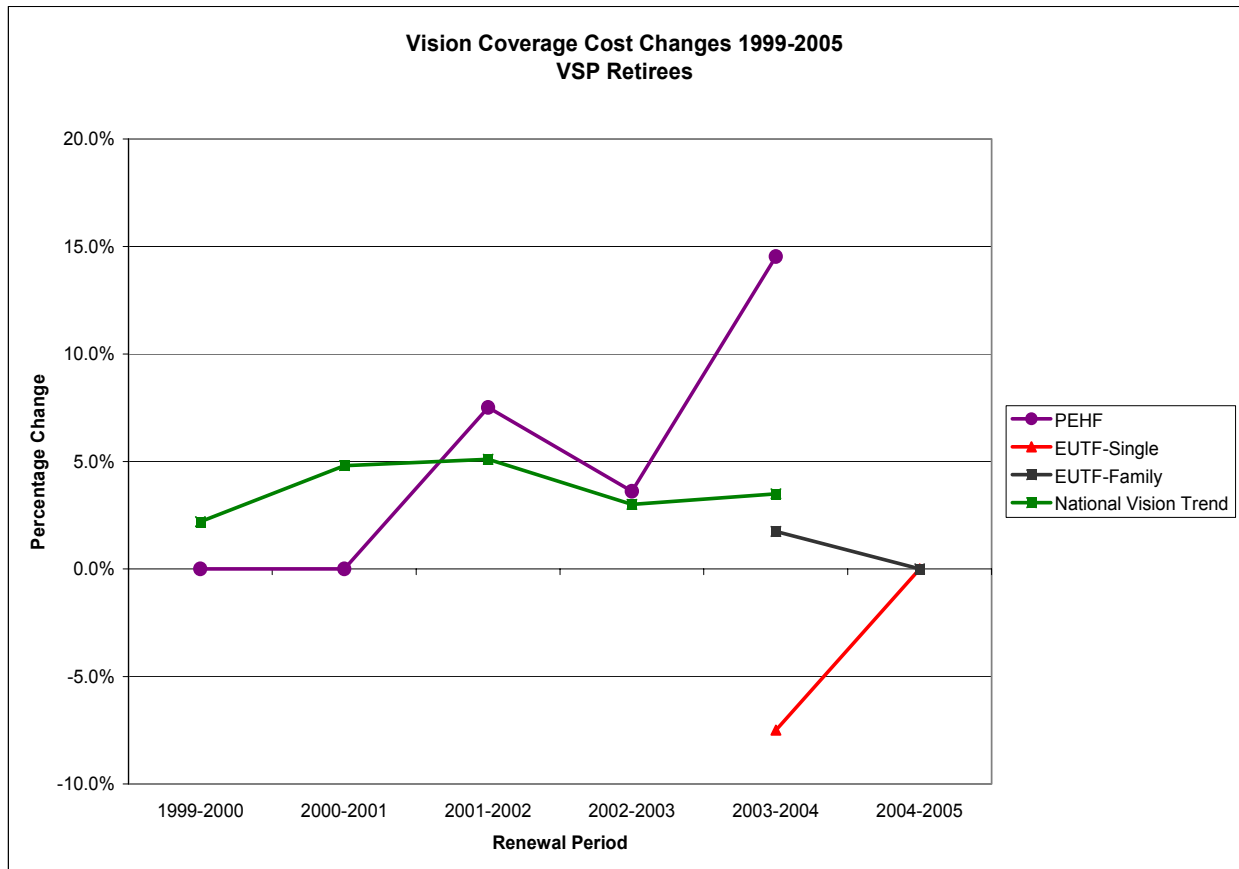
The graph below shows HDS' rate increase percentages for retirees compared to national trend data for dental plans. PEHF rate increases in recent years were less than the national average, but would have been close to the national average if the PEHF had been extended for another year. The EUTF rates in 2003-2004 are lower than the PEHF rates in 2002-2003 and 9.2% less than the PEHF rates would have been. The total first-year savings are \$1,300,752.



Vision Service Plan's rate increase percentages for active employees compared to national trend data for vision plans are shown below. PEHF rate increases in recent years have been higher than national averages. EUTF rates for family coverage are higher than the PEHF rates would have been, but the rates for single employees are significantly (7.8%) lower. The rates are guaranteed not to increase in the second year of the contract. The total first-year savings are \$73,011, a total savings of 1.3%.



The chart on this page shows VSP's rate increase percentages for retirees compared to national trend data for vision plans. PEHF rate increases in recent years have been higher than national averages. EUTF rates are lower than both the PEHF rates and the national average increases. The rates are guaranteed not to increase in the second year of the contract. The total first-year savings are \$413,205, a savings of 16.8%.



Exhibits I, II, III and IV show the data upon which the graphs in this section are based.

The EUTF was able to increase life insurance benefits while decreasing premiums. Benefits for active employees increased by 4% and benefits for retirees increased by 5.6% while rates decreased by 1%. We estimate annual savings to be \$44,978.

The EUTF also added a chiropractic benefit for active employees. The annual cost of this benefit is approximately \$1,069,502.

Compared to the rates quoted for the PEHF, in case it had been extended for another year, the EUTF rates represent an annual savings of \$16,699,334, even after accounting for improved medical and dental benefits and the new chiropractic benefit. We believe that the total

administrative savings from carriers are \$1,985,179 for the first year; this represents 57.7% of the EUTF's budget. The balance of \$14,714,155 can be attributed to negotiations based on the leverage of a larger group. Without the benefit enhancements, we estimate the total savings would have been \$22,995,158.

We recognize that the \$16.7 million in savings assumes that all active employees would be enrolled in PEHF plans and know that would not have been the case. Garner Consulting did analyze the activity on active employees only. Using September 30, 2003 enrollment figures, total premiums for actives in 2003-2004 would be \$292,627,800. Total savings attributable to the active employees' premiums are \$9,356,408, a savings of 3.2%. The savings to employers is 60% of the active employee savings, which is \$5,613,845, plus the retiree savings, for a total of \$12,956,771. Without the improved benefits, we estimate total savings for active employees to be \$15,307,046, a savings of 5.2%. The table below shows our savings estimates by employee group and by carrier:

EUTF vs. PEHF		
	Total Savings	Estimated Savings Without Benefit Enhancements
Actives		
HMSA	\$ 10,302,945.84	\$ 12,386,370.35
Kaiser	354,480.96	354,480.96
HDS	(335,067.84)	1,278,618.88
VSP	73,011.48	73,011.48
MBAH	(1,069,502.04)	1,069,502.04
Aetna	30,539.52	145,062.72
Total Actives	<u>\$ 9,356,407.92</u>	<u>\$ 15,307,046.43</u>
Retirees without Medicare		
HMSA	\$ (861,941.04)	\$ (658,935.82)
Kaiser	790,135.68	790,135.68
Total	<u>\$ (71,805.36)</u>	<u>\$ 131,199.86</u>
Retirees with Medicare		
HMSA	\$ 6,534,653.04	\$ 6,622,687.88
Kaiser	(848,317.44)	(848,317.44)
Total	<u>\$ 5,686,335.60</u>	<u>\$ 5,774,370.44</u>
Retirees		
HDS	\$ 1,300,752.00	\$ 1,300,752.00
VSP	413,204.64	413,204.64
Aetna	14,438.88	68,584.68
Total	<u>\$ 1,728,395.52</u>	<u>\$ 1,782,541.32</u>
Total Retirees	<u>\$ 7,342,925.76</u>	<u>\$ 7,688,111.62</u>
Grand Total	<u>\$ 16,699,333.68</u>	<u>\$ 22,995,158.05</u>